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Message Text

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INFO OCT-01 ADP-00 AID-20 EB-11 NSC-10 RSC-01 CIEP-02

TRSE-00 SS-15 STR-08 OMB-01 CEA-02 CIAE-00 COME-00

FRB-02 INR-10 NSAE-00 XMB-07 OPIC-12 LAB-06 SIL-01

L-03 H-03 PA-03 PRS-01 USIA-12 AGR-20 RSR-01 /164 W
---------- 103768
R 170534Z JUL 73
FM AMEMBASSY ISLAMABAD
TO SECSTATE WASHDC 93
INFO AMEMBASSY DACCA
AMEMBASSY KABUL
AMCONSUL KARACHI
AMCONSUL LAHORE
AMEMBASSY NEW DELHI
CINCPAC

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CINCPAC FOR POLAD

E.O. 11652: N/A
TAGS: EFIN
SUBJ: PRICE INFLATION IN PAKISTAN

SUMMARY: PRICE INFLATION IN PAKISTAN HAS RUN AT RATE OF 15-20 PERCENT DURING PAST YEAR, AND IS CONTINUING. INFLATION HERE REFLECTS WORLDWIDE FORCES, AS WELL AS GOP DEFICIT FINANCING, RUPEE DEVALUATION, AND RISING INCOMES IN RELATIVELY PROSPEROUS RURAL AREAS. GOP HAS ADOPTED VARIETY OF MEASURES TO TRY CURB INFLATION, BUT ITS COMMITMENT TO DEVELOPMENT AND WELFARE MEASURES, AND THE NEED TO PUSH AHEAD WITH INDUSTRIAL REVIVAL, LIMIT CAPACITY FOR REDUCING DEFICIT FINANCING TO DAMPEN INFLATION. REPERCUSSIONS LARGELY CONFINED TO URBAN AREAS, WHERE PEOPLE CONCERNED BUT AT SAME TIME
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GNERALLY AWARE OF GOP MEASURES TO COUNTER INFLATION.

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RURAL PROSPERITY LIMITS AREA OF DISCONTENT TO MINORITY GROUPS. POLITICAL IMPLICATIONS, HOWEVER, COULD BECOME MORE SIGNIFICANT IF INFLATION GOES UNCHECKED, AND WOULD BE AGGRAVATED IF OFFSETTING GOOD FORTUNES OF AGRICULTURAL SECTOR WERE TO CHANGE. END SUMMARY.

1. PERSPECTIVE: IN PREVIOUS REPORTS WE HAVE CALLED ATTENTION TO RISING COST OF LIVING IN PAKISTAN, IDENTIFYING THIS AS A MAJOR PROBLEM ON ECONOMIC FRONT CONFRONTING GOP. SUBJECT ALSO BAS POTENTIAL POLITICAL IMPLICATIONS. PRICE INFLATION HERE REFLECTS IN PART PATTERN OF INFLATION THROUGHOUT MOST OF WORLD. IT IS SOMEWHAT SHARPER THAN IN MOST DEVELOPED COUNTRIES, BUT IS QUITE MODERATE WHEN COMPARED WITH SOME DEVELOPING COUNTRIES. CURRENT RATE OF INFLATION IN PAKISTAN, PROBABLY BETWEEN 18-20 PERCENT PER ANNUM, IS ONE OF HIGHEST PAKISTAN HAS EVER EXPERIENCED.

2. EXTENT OF PRICE INFLATION: IN APRIL 1973 THE OFFICIAL GENERAL CONSUMER INDEX FOR KARACHI STOOD ABOUT 18 PERCENT ABOVE THAT FOR APRIL 1972, WHILE FOR LAHORE THE PERCENTAGE INCREASE WAS NEARLY 19 PERCENT. (THE INDICES HAVE NOT BEEN REVISED FOR MANY YEARS, AND NEED REVISION, BUT REPRESENT ONLY OFFICIAL STATISTICS AVAILABLE) SURVEYS CONDUCTED BY CONGENS KARACHI AND LAHORE FOR JUNE SHOW PATTERN OF CONTINUING INCREASES, APPARENTLY MORE EMPHATIC IN KARACHI THAN LAHORE. IN LAHORE, ONLY A FEW FOOD ITEMS APPEAR TO HAVE SHOWN LARGE INCREASES SINCE APRIL (RICE, BUTTER AND ONIONS); IN KARACHI A WIDE RANGE OF ITEMS SHOWS SIGNIFICANT INCREASES, PARTICULARLY RICE, BEEF, MUTTON, EGGS, POPLIN AND COTTON LONG CLOTH. SOME ITEMS, LIKE KEROSENE AND TEA, HAVE SHOWN REMARKABLE STABILITY. (WHILE LAHORE INDEX RUNNING AHEAD OF KARACHI FOR PAST YEAR OR SO, WE UNDERSTAND DOWNWARD REVISION WILL ALTER THIS.)

3. FACOTRS BEHIND INFLATION: INFLATION HAS BUILT UP STEADILY SINCE INDO-PAK WAR OF LATE 1971. RESORT TO LARGE-SCALE DEFICIT FINANCING HAS BEEN IMPORTANT
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CONTRIBUTORY FACTOR. IN EARLY 1972, SHORTLY AFTER BHUTTO GOVERNMENT TOOK OVER POWER, LARGE INCREASES IN MONEY WAGES WERE NEGOTIATED WITH URBAN WORKERS AND PUBLIC EMPLOYEES. SUCCESSIVE INCREASES IN GOVERNMENT WAGE AND SALARY PAYMENTS WERE ANNOUNCED IN MARCH AND APRIL 1973, AND OTHERS ARE NOW UNDER CONSIDERATION. GOP HAS ALSO ANNOUNCED NUMBER OF SIGNIFICANT COMPULSORY FRINGE AND CASH BENEFITS FOR INDUSTRIAL LABOR.

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THIS HAS BEEN MATCHED AND SUPPORTED BY INCREASES
DURING FY-73 IN RURAL INCOMES, RELFECTING GOOD YEAR
FOR MAJOR CROPS OF WHEAT AND COTTON, AS WELL AS RICE
AND OTHERS. IT HAS ALSO BEEN PARALLELLED BY STEADY
INCREASE IN MONEY SUPPLY, WHICH ROSE BY ABOUT 20 PERCENT
DURING FY-73. THE SHARP DEVALUATION OF RUPEE IN MAY
1972 (FROM RS. 4.76 TO RS. 11.00 -- LATER ADJUSTED TO
RS. 9.90 -- PER DOLLAR) HAD USUAL INFLATIONARY EFFECTS
DURING ENSUING MONTHS. (THIS WAS PRICE TO PAY FOR
AN OTHERWISE VERY DESIRABLE RATIONALIZATION OF FOREIGN
EXCHANGE SYSTEM.)

4. GOP MEASURES: GOP HAS BEEN VERY CONCERNED, PARTICUL-
LARLY AT TOP POLITICAL LEVELS, WITH STEADILY RISING COST
OF LIVING. VARIETY OF COUNTERMEASURES HAVE BEEN TAKE,
SUPPORT PRICES, RATIONING, AND SUBSIDIES HAVE BEEN
APPLIED TO CERTAIN MAJOR ITEMS. THE GOP PURCHASE
PRICE FOR WHEAT FROM GROWERS WAS RAISED FROM RS. 20.00
TO RS. 22.50 PER MAUND, WHILE "ATTA" (FLOUR) CONTINUES
TO BE SOLD AT SUBSIDIZED RATE OF RS. 17.50 AT RATION
DEPOTS. HIGHER PRICES ARE BEING PAID SUGARCANE GROWERS.

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FOR BOTH WHEAT AND SUGAR, IMPORTS HAVE BEEN INCREASED TO COUNTER SHORT SUPPLY SITUATION. IMPORTS OF VEGETABLE OILS HAVE BEEN MADE AND PRICES SUBSIDIZED. EXPORT DUTIES HAVE BEEN IMPOSED ON COTTON AND YARN TO HELP CURB RISING PRICES FOR CLOTH. GOVERNMENT-CONTROLLED UTILITY RATES AND PRICES FOR FERTILIZER AND NATURAL GAS HAVE BEEN KEPT ARTIFICIALLY LOW, EVEN THOUGH ECONOMICS OF SITUATION WOULD LOGICALLY CALL FOR INCREASES TO MATCH DEVALUATION; THE GOP IS HOWEVER MAKING SUCH RATE AND PRICE ADJUSTMENTS ON GRADUAL BASIS. EXHORTATIONS AND THREATS HAVE BEEN LEVELLED AT TRADING SECTOR TO TRY TO CURB SPECULATION AND SMUGGLING. OVERALL, HOWEVER, GOP'S CAPABILITY TO STEM INFLATION IS QUITE LIMITED. GOP'S COMMITMENT TO WIDE RANGE OF WELFARE AND DEVELOPMENT MEASURES, COUPLED WITH NEED TO PRESS
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FOR FURTHER INDUSTRIAL REVIVAL, LIMIT ROOM FOR REDUCING DEFICIT FINANCING TO DAMPEN INFLATION. IN JUNE 1973 PRESIDENT SET UP COMMISSION TO EXAMINE RISE IN PRICES AND TO MAKE RECOMMENDATIONS FOR PROVIDING RELIEF. CHAIRMAN IS FORMER FINANCE MINISTER (END OF AYUB PERIOD) UQAILI. CONGEN KARACHI REPORTS THAT UQAILI HAS PRIVATELY OBSERVED THAT TERMS OF REFERENCE OF COMMISSION ARE TOO LIMITED, AND BELIEVES BROADER AND MORE FUNDAMENTAL LOOK SHOULD BE TAKEN AT WHOLE PROBLEM OF PRICE STRUCTURE IN PAKISTAN ECONOMY, WHICH HE REFFERED TO AS "PATCHWORK OF CONTROLS AND NEGLECT." UQAILI ALSO SAID ELEMENTS OF PRIVATE SECTOR OFTEN UNFAIRLY CRITICIZED BY GOP AS BEING MALICIOUS HOARDERS.

5. REPERCUSSIONS OF INFLATION: CONGEN KARACHI REPORTS "GENERAL TONE OF COMMENTS WE HAVE HEARD IS ONE OF FAIRLY STRONG CONCERN -- BUT NEITHER DESPAIRING NOR BITTER." CONGEN LAHORE REPORTS "PEOPLE ARE BECOMING WORRIED, PARTICULARLY THOSE IN FIXED INCOME GROUP..." AND BELIEVES CONCERN MIGHT BE SOMEWHAT GREATER THAN REPORTED BY KARACHI. SITUATION OF URBAN WORKERS IS ALLEVIATED BY PUBLIC AWARENESS OF GOP MEASURES TO AMELIORATE SITUATION. BOTH CONGENS HIGHLIGHT FACT THAT VAST RURAL AREAS RELATIVELY UNAFFECTED BY PRICE INFLATION: RURAL PROSPERITY IN SOUTHERN SIND AT LEVELS NOT SEEN IN TEN YEARS; IN COUNTRYSIDE PUNJAB WHERE CROPS ARE GOOD PEOPLE ARE RELATIVELY UNTOUCHED BY

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PRICE PROBLEM. IN CONTEXT GOOD CROPS AND BOOMING
WORLD MARKETS FOR PAKISTAN'S MAJOR EXPORT ITEMS --
COTTON (RAW, YARN AND MANUFACTURES) AND RICE -- INFLA-
TION IS A PROBLEM LARGELY LOCALIZED IN URBAN AREAS.
ARE THERE APPARENT POLITICAL IMPLICATIONS IN INFLATION?
NOT AT THE MOMENT, AS BOTH CONGENS CONCUR, BUT
POTENTIALLY SO IF INFLATION GOES LONG UNCHECKED. IMPACT
OF INFLATION WILL CONTINUE TO BE CUSHIONED AS LONG AS
CROPS CONTINUE GOOD AND EXPORT MARKETS STRONG.

6. CONTRIBUTIONS: KARACHI 1125 AND LAHORE 0794, ON
WHICH WE HAVE DRAWN FOR THIS REPORT,ARE BEING POUCHED
NEA/PAB. BOTH ARE HIGHLY USEFUL REPORTS AND WILL
PROVIDE SUPPLEMENTARY DATA AND DETAILS TO NEA END-USERS.
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